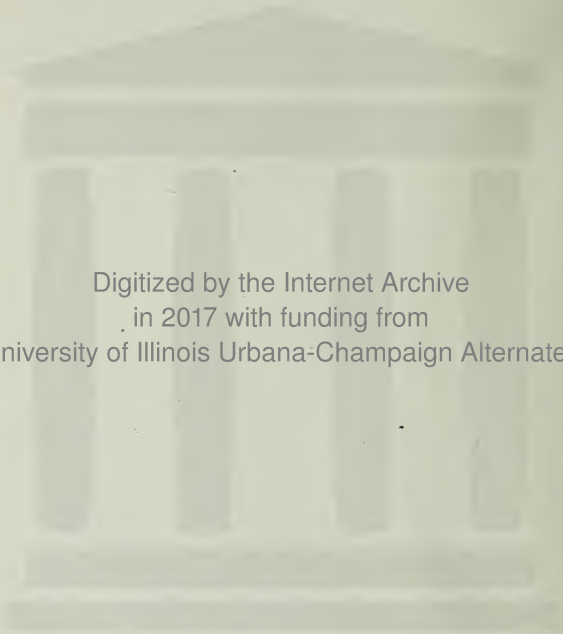
Comments on the Workmen's Compensation Bill Recommended in the Majority Report of the Iowa Employers' Liability and Workmen's Compensation Commission

A Letter to Welker Given, Esq., Secretary Iowa Employers' Liability and Workmen's Compensation Commission, from

P. Tecumseh Sherman, of
New York



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November 8, 1912.

Welker Given, Esq., Sec'y,
Employers' Liability and Workmen's Compensation Commission,
State Capitol,
Des Moines, Iowa.

My Dear Mr. Given:

After a detailed study of the bill recommended by the majority of your commission and of the minority report of and bill recommended by Mr. Baldwin, copies of which you were kind enough to send me, I write to present my criticisms thereof as follows:

Where "compensation" is elected the scheme of the bill recommended by the majority is as follows:

The employer is made directly liable to his injured workmen to compensate them for their injuries (Sec. 10). And each injured workman is given a general lien on all property of his employer for the amount of the compensation (Sec. 20)—which lien is not discharged by insurance. The employer is required to join a state-wide employers' mutual insurance association to assure the payment of the compensation to his injured workmen (Sec. 48). That association must distribute its members into groups, and fix the rates of premiums for the groups and individuals; it must place 10% of premiums collected in a reserve until the amount therein reaches $1,000,000; and until the reserve amounts to $100,000 the association must reinsure "the risks of its members" in certain amounts roughly proportionate to the number of employees insured at the time (Sec. 50). Voting rights are fixed in Sec. 49. With these exceptions the association is left to settle its By-laws and methods and practices of administration for itself. The right to and amount of compensation may be adjusted either by agreement between each injured workman and his employer

or by suit before a "Committee of Arbitration" (Secs. 28-33), subject to review on appeal to the "Iowa Industrial Commission" (Secs. 24, 26, 34),— the determination of which novel tribunals are to be enforced by the courts (Sec. 35).

I respectfully submit that there are serious objections:

(1) To the lien.
(2) To this form of compulsory insurance.
(3) To the provisions for reserves.
(4) To the provisions for reinsurance.
(5) To the provisions for adjustment of compensation.
(6) To the machinery for arbitrations.

The objections, briefly presented, are as follows:

(1) The workman's lien is a blanket first lien (Sec. 20), prior in law to all other liens (even to those prior in time) that may attach after the act takes effect. Such a lien would inevitably destroy credit and drive capital out of industry; and it would almost continuously tie up the funds of larger employers. There is no justification for such a lien under any circumstances, and not even an excuse for a lien where insurance is compulsory.

(2) This bill forces employers in all trades and occupations into one blind pool, and gives to the controlling factions in that pool the power to tax all the members about as they choose, upon the hypothesis that such power will be exercised properly, fairly and to general satisfaction. But experience is contrary to that hypothesis. In Austria, for example, where practically all the employers in each of the territorial districts are forced into the same association, the more hazardous trades, by use of their voting power, have succeeded in avoiding adequate rates for themselves, to the prejudice of the less hazardous trades. It should be obvious from experience that in a mutual association, composed of elements with discordant interests, there will be nothing like unanimity of opinion as to rates, practices, etc., and, consequently, that there will be bitter struggles in regard thereto, and that "blocs" or combinations will be formed to secure control so as to use the power of control to impose an unfair share of the cost on the minority.

Even if the membership of a mutual association be substantially harmonious, mutual insurance engages the members in a side business in which they are not expert, and which consequently involves unusual peril of technical mistakes, besides entailing on its officers and members much unremunerated labor, that will interfere with their regular occupations. If the administration be expert and efficient and in large part unpaid, mutual insurance may be cheaper than

bought insurance. But that "if" implies grave uncertainty. Mutual insurance, therefore, should be permissible, but not compulsory.

Consider the concrete problem involved in the organization of the proposed association. The employers who elect compensation will promptly be called to a meeting to perfect their organization (Sec. 48). There is no provision for delegates or proxies;—the employers must meet personally. And to protect their respective interests they must remain in conference until all the complex matters vitally affecting those interests are settled. They will find a temporary organization in control for one year (Secs. 44, 45); but they must in effect frame the permanent organization then and there; and they must frame it correctly, without a single vital administrative or actuarial defect, at their peril. A voluntary organization would employ experts and give them plenty of time to frame the details of a plan for mutual insurance, and then would consider the plan long and carefully before adopting it. But this bill compels employers to reverse the natural process, pitches them at once into a partnership of losses, and then leaves them to settle the vital details in haste and as best they may. That such a method would result in generally satisfactory mutual insurance is most improbable. The adoption of such a method, therefore, would amount in effect to an invitation to all careful employers not to elect compensation—which would be most unfortunate.

This bill contemplates that one mutual insurance association shall provide insurance for both industrial and agricultural labor. The practical objections to that are overwhelming. Foreign experience demonstrates that premium rates for agricultural accident insurance cannot be based upon wages, and that in agriculture it is almost impossible to distinguish between hired help and family help, and between work accidents and other accidents, and consequently that agricultural accident insurance must be provided in a different form and on a different basis from industrial insurance. Therefore, unless these two radically different branches of insurance be kept distinct, agriculture will mulct industry, or vice-versa.

This bill requires all employers who elect compensation to insure. But railroads and great proprietors with many establishments, having their risks well distributed, do not need to insure. And to compel them to do so, simply to round out a paper scheme, would be an imposition upon them. Likewise would it be an imposition upon employers in other states, who occasionally send their workmen into Iowa, to compel them either to insure in this proposed state mutual association or to remain out of the compensation law.

Strongest to me of all objections to this bill is that it creates a monopoly. Thereby you would eliminate the expenses of competition from the cost of

insurance; but that saving would be more than offset by the loss in efficiency that would inevitably result from the absence of the stimulating effects of competition. I will not argue the issue between monopoly and competition, but will merely emphasize my opinion that there is no more reason for monopoly in the insurance of compensation than in fire or life insurance or in retailing foodstuffs or in manufacturing staples.

In brief, if this scheme is designed to avoid trouble and to reduce the cost of insurance for employers, it is singularly ill adapted to its purpose. If compulsory insurance be deemed necessary in order to assure the payment of compensation to the injured—which proposition is contrary to English experience —then the Michigan law should be followed. Although it has some defects it presents a better plan than this.

(3) The provision of Sec. 50 requiring that 10% of premiums be placed in a reserve is valueless. Mutual insurance must either be conducted on the deferred assessment basis or must carry reserves to cover outstanding liabilities. If conducted on the deferred assessment basis, employers must be liable to the association for deficiencies and must be obligated to continue their membership and not be left free to drop out—otherwise the insurance will be unsound. If, on the other hand, reserves are to be maintained, it is not sufficient to place any arbitrary proportion of premiums, such as 10%, in the reserves; but the capitalized values of all outstanding liabilities must be estimated or computed and an amount sufficient surely to cover them must be transferred from premiums to reserves—whether that amount be 10% or 50% of premiums. And another reserve must be carried to cover the liability for unearned premiums. And experience demonstrates that the amount to be transferred to such reserves will be nearer to 50% than to 10% of the first year's premiums—unless those premiums are heavily loaded. Consequently this Iowa plan follows neither of the correct methods of insurance. Suppose that only 10% of premiums should be placed in reserves, and that at the end of several years the mutual association's outstanding liabilities should be about $1,000,000, and the amount of its reserve fund should be only $100,000, then the majority of employers could elect to reject the compensation liability (Sec. 1) and could drop out of the mutual association—whereupon the insurance scheme would collapse. It is true that many of the employers who had insured in the scheme would then still be bound by their direct liabilities to their injured workmen and consequently would be unable to escape by dropping out of the mutual insurance association. But very many others would be more lucky. And if the latter only should secede it would be sufficient to ruin the scheme.

(4) The provisions in Sec. 50 for reinsurance are curious, and I must confess that their meaning and purpose are beyond my ability to comprehend.

The need for reinsurance and the amount of reinsurance requisite for safety are in inverse ratio to the number and distribution of the risks insured. In other words, if I insure 500 employees in one establishment at a given rate I have a greater need for reinsurance and a need for a greater amount of reinsurance, than if, at the same rate, I insure 50,000 employees distributed in many establishments. But Sec. 50 requires the mutual association to reinsure in proportion to the number of its risks—for which there is no sound reason.

And what does Sec. 50 of this bill mean where it requires the mutual association, when its membership represents 25,000 employees, to reinsure "the risks of its members" in the amount of $50,000, "which shall be for the use and benefit of the association to meet its liabilities and liabilities of its members when needed to pay the compensation contemplated by the Act?" Does it mean that $50,000 shall be spent in premiums for as much reinsurance as can be bought therefor, or that reinsurance with a $50,000 limit shall be purchased? Whichever is meant, only partial reinsurance can be purchased—not reinsurance covering all the risks of the members. Then, what specific part of the risks shall be reinsured? On these questions the provision is either ambiguous or wholly indefinite. Consequently its meaning and purpose are uncertain, and its effect would be harmful.

The required reinsurance, it is further provided in Sec. 50, shall be purchased from private insurance companies. But such reinsurance would be extravagantly expensive; for it is the purpose of this scheme to drive private companies out of business, and consequently there would be no inducement for them, in the way of a prospect of continued business, to offer bargain rates or anything but the most profitable rates. Of course defective reinsurance might be purchased at apparently low rates; but such insurance is neither really cheap nor profitable.

In no way therefore, do these provisions for reinsurance tend to strengthen the scheme of insurance provided for in the bill. Either that scheme should be designed to be always self sustaining, so as to avoid, if possible, the necessity for reinsurance; or its managers should be left free to reinsure or not, and to reinsure in such manner and in such amounts, as conditions warrant.

(5) The bill provides that the amount of compensation due may be adjusted either by agreement between the injured workman and his employer (Sec. 27), or by suit in the arbitration courts by the workman against the employer (Secs. 28-35). But it is the mutual association and not the employer that primarily

must pay the compensation. Therefore that association should have some check upon the power of the employer to admit claims which it must pay, and some standing in arbitration proceedings to adjust such claims. For foreign experience demonstrates that insured employers will sometimes unduly favor their workmen at the insurer's expense.

(6) The machinery provided for adjusting disputed claims—namely the Iowa Industrial Commission (Secs. 24-26, 34) and the Committees of Arbitration (Secs. 28-33)—is cumbersome and expensive and a useless duplication of appropriate existing machinery—i. e., the courts. Under that procedure in order to settle a dispute the parties must each name an arbitrator, and then call upon the Industrial Commission to send down one of its three members to sit as third arbitrator and chairman. The three members of the Industrial Commission will be wanted on arbitration committees constantly in all parts of the state and besides will have to sit frequently "in banc" to hear appeals. Consequently the hearings of the various arbitration committees can no more be fixed to suit the convenience of parties than can terms of court; but each committee must fix its sessions to suit the convenience of an itinerant commissioner. From the decision of any such committee an appeal lies to the Industrial Commission, which commission may proceed to try the case de novo, and for that purpose may summon the parties and their witnesses to Des Moines. The practice and procedure of these new tribunals remain to be formulated and to become settled and familiarly known, before they can work as smoothly as those of the courts. And before any decision by these tribunals can be enforced the record must be transferred to a court and a decree entered thereon by the court. There is no advantage to be gained by thus substituting one kind of courts in the place of another kind of courts; for questions of law and fact will still arise, which must still be tried in about the same way as in courts—or general injustice and ruinous abuses will almost inevitably result. The best results in the way of cheapness, expedition, etc., in adjusting disputes are obtained under the English compensation law. Under that law the parties may voluntarily submit disputes to arbitration—standing boards of arbitration in organized industries being the most successful—or may force their cases to trial before a judge of the proper County Court, acting as arbitrator and under summary procedure, with a right of appeal from his decision only upon questions of law. In my opinion it *certainly* would be far more advantageous for the State of Iowa to increase its judicial force and to amend its judicial procedure as may be necessary to enable its courts to deal with compensation disputes according to the English practice, rather than to start in the way of duplicating its judicial force, as in this bill proposed.

The following are minor criticisms of the bill, and suggestions for corrections or improvements.

(A) This law is to apply "where five or more employees * * * are employed in the same general employment and in the usual and ordinary transaction of the business." (Sec. 1, a). That provision is not sufficiently definite, but will give rise to much uncertainty and litigation. For example does a farmer who usually and ordinarily employs a dozen men for harvesting, and during the remainder of the year employs only two, come under the law?

(B) The scale of compensation is placed at 60% of wages or of wage loss (Sec. 10, h-i). There is no principle for such a scale, unless workmen contribute. Fifty per cent. of wage loss (proportionately increased where workmen contribute or where limitations are low) is the prevailing scale. And that scale is based upon reason, namely the idea that employers and workmen on the average are jointly and equally responsible for accidents, and that by making them suffer the consequences of injuries equally there will be created the greatest incentive for accident prevention. If the scale be placed too high malingering over trifling accidents will be encouraged among certain classes; for it must be remembered that there exists a small proportion of workmen who are shiftless and generally out of a job, and for whom 60% of wages may mean more than 100% of their average earnings. This class will seek for pensions in preference to employment and wages; and compensation schemes with high-rate pensions are liable to be ruined by the drain from such parasites. It would be more liberal and far more beneficial to reduce the scale of compensation to 50% and to offset that reduction by lengthening the limitations from 300 to 400 weeks for temporary disability and from 400 to 500 weeks for permanent total disability.

(C) Sec. 10 (j) is wholly indefinite as to whether the life pension shall be $10 or $25 a month. That is a serious defect, and would make the cost of insurance forever uncertain and incalculable. That pension should be fixed at a certain percentage of wages or at a sum certain—just sufficient to prevent indigency.

(D) Sec. 10 (k) furnishes no definite rule for calculating pensions for partial disability. That is a serious defect, for partial disabilities are very numerous. The rule should be so definite that, with the facts ascertained, employer and employee will ordinarily be guided thereby to a mutual agreement as to the correct amount. In my opinion, generally the pension should be 50% of the estimated wage loss.

(E) In my opinion the first eleven items in the schedule of rates for specific injuries contained in Sec. 10 (k), while conducive to prompt settlements,

are improper. For example, the loss of a first finger may be a vital loss to a workman in some of the skilled trades, which loss would not be fairly compensated for by 60% of wages for 30 weeks. And what would be the rule if a man loses three, four or all of his toes, or parts of them? Would his compensation be a multiple of the rates for the specific injuries covered in this schedule? And if so, who can contend that the amount would be reasonable? And suppose that a workman loses a part of a finger or a toe, and thereby becomes entitled to a pension for a certain number of weeks;—would he then remain idle for all those weeks although he has entirely recovered much earlier? Or would he return to work and for some weeks receive full wages plus 60%? In my opinion, based upon experience, this part of the schedule would cause idleness or waste, and constant dissatisfaction over its results in particular cases. Would it not be better to give the workman who suffers any of these specific injuries ordinary compensation while disabled plus some reasonable lump sum as compensation for his permanent injury?

(F) It is provided in Sec. 33, relative to arbitrations, that "in the event of the employer being the losing party" he shall pay costs, including an attorney's fee—not to exceed $50. Now in about 99.9% of compensation cases the dispute is solely about the *amount*, and the employer is always the losing party, in the sense that the award is against him. This provision had better be made certain *now*, before the "ambulance chasers" get organized and established, so that an employer shall be liable for costs and attorneys' fees only when an amount substantially higher than what he admits to be due be awarded against him. Otherwise, the proportion of claims that will be litigated will be enormous and the cost thereof to employers will be ruinous.

(G) Section 34 provides for a review of the decision of an arbitration committee whenever claimed by either party. That offers opportunities for grave abuses. Where the decision of a committee of arbitration is unanimous there should be no right to review.

Turning now to Mr. Baldwin's minority report, I must say that, with some comparatively unimportant qualifications and exceptions, I agree with it entirely. His bill does not purport to be fully formulated, and consequently, although it contains some provisions which I think might be improved, it is hardly appropriate to enter into a detailed criticism of it at present.

With renewed thanks for courtesies received from yourself and the members of your commission, I am,

Very truly yours,

P. TECUMSEH SHERMAN.